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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1964

No. 326

ARTHUR W. SLOAN, FRANKLIN C. SALISBURY, AND ATLANTIC RESEARCH CORPORATION, *Petitioners,*

v.

SAMUEL MELTZER, *Respondent.*

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT.

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v.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FOURTH CIRCUIT.

Petitioners, Arthur W. Sloan, Franklin C. Salisbury, and Atlantic Research Corporation, pray that a writ of certiorari be issued to review the judgment of the United States Court of Appeals for the Fourth Circuit, entered in the above entitled cause on April 9, 1964, rehearing denied May 21, 1964.

Opinions Below

The opinion of the Court of Appeals for the Fourth Circuit is reported in 330 F. 2d 946, and printed as Appendix A of this petition. The opinion of the United States District Court for the Eastern District of Virginia, Alexandria Division, dated May 29, 1963, is printed as Appendix B of this petition.

Jurisdiction

The decision of the Court of Appeals setting aside the judgment of the United States District Court for the Eastern District of Virginia, Alexandria Division, was entered on April 9, 1964. A timely petition for rehearing was filed on May 7, 1964, and was denied on May 21, 1964. The order denying rehearing is printed as Appendix C of this petition. The jurisdiction of this Court is invoked under 28 U.S.C. §1254.

Question Presented

Where the plaintiff-shareholder admits on deposition that a demand upon a board of directors was not even considered prior to the filing of the complaint in a purported derivative shareholders' suit, can the plaintiff-shareholder nullify Rule 23 (b) of the Federal Rules of Civil Procedure, which requires this administrative remedy be exhausted, by naming each individual director a defendant in such action and making general charges of complicity in wrongdoing against the directors as a group?

Federal Rule of Civil Procedure Involved

The Rule in question is Rule 23 (b) of the Federal Rules of Civil Procedure (28 U.S.C. following §2072). The Rule states as follows:

> "(b) Secondary action by Shareholders. In an action brought to enforce a secondary right on the part of one or more shareholders in an association, incorporated or unincorporated, because the association refuses to enforce rights which may properly be asserted by it, the complaint shall be verified by oath and shall aver (1) that the plaintiff was a shareholder at the time of the transaction of which he complains or that

his share thereafter devolved on him by operation of law and (2) that the action is not a collusive one to confer on a court of the United States jurisdiction of any action of which it would not otherwise have jurisdiction. The complaint shall also set forth with particularity the efforts of the plaintiff to secure from the managing directors or trustees and, if necessary, from the shareholders such action as he desires, and the reasons for his failure to obtain such action or the reasons for not making such effort."

Statement

Respondent (plaintiff and appellant below), the owner of 100 (out of 1,900,000 issued) shares of Atlantic Research Corporation (Atlantic) filed an original complaint on November 13, 1962, against the Corporation and each individual member of the Board of Directors. On January 3, 1962, Respondent filed an amended complaint, which alleged chiefly that defendant Scurlock, then President of Atlantic, diverted some $3,900,000 of Atlantic's money by loaning the $3,900,000 to various companies controlled by himself or defendant Sloan. Those companies then allegedly used the money to buy Atlantic's stock on the open market. It was alleged that, as security for these loans, Atlantic stock was pledged and that, because of a decline in market price of Atlantic's stock, Atlantic may lose several million dollars.

The original complaint in paragraph 15 and the amended complaint in paragraph 20 attempt to excuse the failure to make the demand upon Atlantic's Board of Directors, or shareholders, which is required by Rule 23 (b) of the Federal Rules of Civil Procedure, by the following allegations:

"(a) The Board of Directors is controlled and dominated by the alleged wrongdoers, through their offi-

cial positions with Atlantic, and by virtue of their very substantial holdings;

(b) The Directors have participated in the wrongs alleged;

(c) The Directors have negligently permitted the aforementioned wrongs to occur and are liable therefore; and

(d) The institution of this action by the directors would place it in hostile hands and would prevent its effective prosecution."

The testimony in the record herein demonstrates these allegations are false. The District Court expressly found that the facts established by testimony under oath conclusively disproved the complaint's allegations (Appendix B, p. 40). The Court of Appeals overruled this factual finding and reversed on the basis of the disproved allegations of the amended complaint (Appendix B, p. 23).

The amended complaint is based chiefly on orders of the Securities and Exchange Commission (SEC) beginning with an order suspending trading in the stock of Atlantic issued on October 10, 1962. Subsequently, on November 7, 1962, the SEC issued an order authorizing the institution of proceedings with respect to a registration statement of Atlantic filed in July, 1962. On November 9, 1962, the SEC's "Statement of Matters" issued in connection with such proceedings was made public. On November 9, 1962, the Board of Directors of Atlantic mailed all shareholders of Atlantic the SEC "Statement of Matters" as well as a Special Report. This Report set forth the details of many of the transactions which gave rise to the

SEC's action and recited various corrective measures which were being undertaken by Atlantic's management (Appendix F, p. 59). Such measures, as found by the District Court, included among others: (1) Increasing the Board of Directors by electing two new outside directors, (2) Authorizing an Executive Committee of three members of the Board, two to be outside directors; (3) Realignment of the executive officers of Atlantic so as to remove defendant Scurlock as President and naming both a new Chief Executive Officer and a new President; (4) Retaining, for the first time, an outside law firm as general counsel; (5) Retaining a new accounting firm; (6) Finding and engaging a person well versed in corporate finance as Treasurer; (7) Action to pledge additional security for certain bank loans; (8) A guarantee by defendants Scurlock and Sloan against loss by Atlantic on the questioned loans owed to Atlantic from various companies plus a pledge of the stock purchased with the loaned money and a second mortgage. See affidavit of Atlantic's Secretary (Appendix E, p. 53).

The District Court found that these major remedial steps clearly indicated that, at the time it would have been appropriate for the plaintiff below to make a demand on the Board, an independent and disinterested majority of the Board were in charge of the Corporation's affairs. Under these circumstances, a demand on the part of the plaintiff below would not have been futile. The District Court so found. (Appendix B, p. 39-40).

Respondent testified that he signed the original complaint on November 10, 1962, before he received the Special Report, dated November 9, 1962. Respondent, by his own admission, did not consider or even discuss with his counsel the matter of making demand on Atlantic or its Board of Directors that it take remedial actions to remedy his alleged complaint as to which he testified he knew of

no damage actually suffered by Atlantic (Appendix D, p. 51). He testified:

Q. "When you contacted your counsel, did he suggest to you that you contact Atlantic Research for an explanation of this matter before you filed a lawsuit?

A. "No. It was not necessary. The whole story was known to everybody by the press.

Q. "He did not suggest to you that you make a demand upon the officers or directors or the stockholders of Atlantic Research?

A. "No, he did not.

Q. "Did he say anything to you about making such a demand and waiting 60 days before filing your lawsuit?

A. "Not that I recall, no.

Q. "This demand was not discussed at all, then?

A. "No, sir.

* * * * * * *

Q. "Was it your decision not to contact the Corporation or its officers and directors and other stockholders before filing this lawsuit, or just whose decision was it?

A. "It was my decision.

Q. "And you say you did not even discuss it with your attorneys?

A. "No." (Appendix D, p. 51).

Moreover, although before filing his amended complaint on January 3, 1963, Respondent received the Special Re-

port which outlined the remedial actions taken by Atlantic referred to above, he testified he did not pay much attention to it. (Appendix D, p. 51-52).

Proceedings Before The District Court

The defendants below, after taking plaintiff's deposition, moved to dismiss the complaint on the ground that the plaintiff below had failed to make a demand for the remedial action he seeks upon Atlantic's Board of Directors as required by Rule 23 (b) of the Federal Rules of Civil Procedure. The District Court held a hearing at which it considered the extensive testimony of plaintiff on this issue. The District Court in its findings of fact and opinion took special note of plaintiff's testimony that he did not even consider making a demand upon the Board of Directors prior to the filing of the complaint. (Appendix D, p. 51). The District Court, in dismissing the complaint without prejudice to refiling after compliance with Rule 23(b), properly reasoned that, "if this plaintiff can say that he does not know whether the remedial action is all that he wanted, it ill behooves him to come into the court and ask the court to tell him." (Appendix D, p. 40). See also testimony in Appendix D, p. 51.

Proceedings in the Fourth Circuit.

The Respondent appealed the ruling of the District Court to the United States Court of Appeals for the Fourth Circuit. The Court of Appeals held that a demand on the Board of Directors would have been in vain and ineffectual. (Appendix A, p. 21). The Court of Appeals reasoned that, despite the contrary testimony of plaintiff before the District Court, *supra* page 6 the general allegations of the complaint quoted above should be treated

as admitted. The Court of Appeals, therefore, reversed the factual findings of the District Court and reversed the District Court's decision based thereon.

REASONS FOR GRANTING THE WRIT

I. The Issue Involved in This Case Is One of National Importance

The issue involved in this case is one of national importance because it affects a large volume of litigation in both Federal and state courts. It calls for the exercise by this Court of its supervisory powers to insure that the purpose of the Federal Rules of Civil Procedure is adhered to by the federal court system. The effectiveness of Rule 23(b) will be nullified if the decision of the Court of Appeals is not reversed. That Court's decision is in direct conflict with the clear, express purpose of the Federal Rules of Civil Procedure. This purpose is to secure the just, speedy and inexpensive determination of every shareholder claim initially by those most familiar with the facts, the corporation's Board of Directors. Failure of the Board to act allows the filing of a Court action to secure the relief desired by a shareholder. The shareholder is required to set forth in any court complaint he files, with great particularity, his efforts to secure relief from the Board or the other shareholders. Thus does Rule 23(b) re-emphasize that resort to the Board or other shareholders as a group for remedial action is required before the complaining shareholder has standing to maintain a derivative shareholders' suit in Court. And thus is recognized the fact that such a suit initially belongs to the corporation itself, and that the benefits of such a suit (other than counsel fees) belong to the corporation.

The fact that this Court promulgated the Federal Rules of Civil Procedure as formulated and recommended by the

Advisory Committee does not foreclose consideration by this Court of their validity, meaning or consistency. *Mississippi Publishing Corp.* v. *Murphree*, 326 U.S. 438, 444. The policy envisaged by the enabling act of June 19, 1934,[1] was that the whole field of court procedure be regulated in the interest of speedy, fair and exact determination of the truth. The Rules comport with this policy. *Sibbach* v. *Wilson & Co.*, 312 U.S. 1, 14. This Court has continued its interest in, and supervision of, the Rules by its order making the Advisory Committee a continuing body. 314 U.S. 720. In a whole series of important decisions this Court consistently has upheld the purpose and validity of the Rules and has reversed decisions which conflict with that purpose. See, for example, *Sibbach* v. *Wilson & Co.*, 312 U.S. 1, 13-15; *Mississippi Publishing Corp.* v. *Murphree*, 326 U.S. 438, 445-446; *Sears, Roebuck & Co.* v. *Mackey*, 351 U.S. 427, 436-438; *Cold Metal Process Co.* v. *United Engineering & Foundry Co.*, 351 U.S. 445, 452-453.

This Court's active interest in and supervision of the Federal Rules of Civil Procedure is demonstrated by four orders adopting amendments thereto which have originated by recommendation of the appropriate committees. In 368 U.S. 1019, 1023-1041, this Court extended certain deposition and discovery provisions of the Rules to the rules of practice in admiralty and maritime cases. In 368 U.S. 1014, 1015-1018, Rules 25, 54, 62, and 86 were amended. In 368 U.S. 1044, 1047-1070, considerable clarifying revision of many of the bankruptcy general orders and forms was made. In 374 U.S. 871, 875-900, further clarifying amendments were made to the Rules.

Viewed in perspective, the Federal Rules of Civil Procedure have lived up to their purpose of reducing unneces-

[1] 48 Stat. 1064, 28 U.S.C. § 2072.

sary litigation and improving the administration of justice in the Federal courts by eliminating technicalities and speeding up the disposition of cases. These Rules have been substantially adopted in twenty or more states. Similar rules have been adopted in most of the other states.[2] Consequently, the decision of the Court below will have a broad effect not only in the Federal court system but also in the state courts because of their rules comparable to Rule 23(b).

The Court of Appeals has defeated the salutary purpose of Rule 23(b). It has opened the door to direct court aid to all shareholders who make unsupportable charges against a majority of any board of directors. This decision is contrary to the unambiguous language of the Rule. The decision will encourage a flood of litigation in the Federal and state courts contrary to the purpose of the Rule. Where, as here, there is sworn testimony which is relied upon by the District Court in its findings there is no reason whatever to give broad general conclusory statements in the complaint the status of incontrovertible facts. But the Court of Appeals did exactly that.

A duly authorized rule of Court has the force of law, is binding upon the Court as well as upon parties to an action, and cannot be dispensed with to suit the circumstances of any particular case. *Rio Grande Irrigation & Colonization Co.* v. *Gildersleeve*, 174 U.S. 603, 608-609. The Federal district courts have a wide discretion in interpreting and enforcing civil procedure rules in order that speedy and efficient administration of justice may be secured. *Saxton* v. *W. S. Askew Co.*, 38 F. Supp. 323, 325 (N.D. Ga. 1941). The effect of the decision of the Court

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[2] See Barron & Holtzoff, 1 *Federal Practice and Procedure*, § 9 at 43-80 and 1963 Pocket Part at 19-25.

of Appeals herein takes this discretion away from the District Court and goes even further. It also constitutes the Court of Appeals the trier of facts in violation of Rules 39(b) and 52(a) of the Federal Rules of Civil Procedure.

II. The Purpose and Intent of Rule 23(b) Is To Prevent Unnecessary Litigation

The purpose of the prior demand requirement in Rule 23(b) is to prevent a flood of unnecessary litigation in the courts. The authority to sue for corporate injuries is primarily in the corporate management. When the shareholder sues, not upon an individual right, but a right which properly belongs to the corporation, and to which the fruits of the judgment go, his status—or standing—as a plaintiff is conditional upon his prior request that the primary holder of the right sue. In accordance with public policy, Rule 23(b) requires that the complaining plaintiff should not be able to attempt to control corporate management without first requesting appropriate action by the directors and, if need be, by the stockholders. *Bruce & Co.* v. *Bothwell*, 8 F.R.D. 45, 46-47 (S.D. N.Y. 1948); *Jacobson* v. *General Motors Corp.* 22 F. Supp. 255, 257 (S.D. N.Y. 1938). In the *Jacobson* case, the Court emphasized that "[p]rior demand or its equivalent . . . is a universally accepted principle of equity and has been applied in most federal cases, regardless of their origin or nature." If the board of directors acts within its powers and not wrongfully, a derivative suit cannot be maintained. *Delaware & Hudson Co.* v. *Albany and Susquehanna R. Co.*, 213 U.S. 435, 444, 446-447, 451. This is especially true here where the directors took remedial action which was not even considered by the respondent before he filed his complaint and his amended complaint. Appendix D, p. 51.

In the *Delaware and Hudson* case, it was certified that:

> "So far as appears from anything shown in this record, none of the directors or officers of the Delaware Company ever, before or after bringing this suit, treated the claim therein set forth otherwise than as one of doubtful validity. . . ."

This Court therefore held that, in a situation where "emergencies may arise in which the antagonism between the directors and the corporate interest may be unmistakable . . . the requirements of the [former Equity] rule [94] may be dispensed with." The Court of Appeals decision is clearly in conflict with this Court's rationale in *Delaware & Hudson Co.* Here the directors of Atlantic Research Corporation did take remedial action of great consequence. True, respondent ignored that action, but this does not wipe out the fact that remedial action was taken, and that Respondent received a written report reciting that action prior to the filing of his amended complaint.

The leading case concerning the prior demand requirement by shareholders on boards of directors is *Hawes* v. *City of Oakland*, 104 U.S. 450, 460-462. Rule 23(b) is merely an enactment with minor variance of the original Equity Rule 94 established in the *Hawes* case which later became Equity Rule 27. See *Goldstein* v. *Groesbeck*, 142 F. 2d 422, 425 (2d Cir. 1944).

In the *Hawes* case, this Court declared at page 461:

> "But, in addition to the existence of grievances which call for this kind of relief, it is equally important that before the shareholder is permitted in his own name, to institute and conduct a litigation which usually belongs to the corporation, he should show, to the satis-

> faction of the court, that he has exhausted all the means within his reach to obtain, within the corporation itself, the redress of his grievances, or action in conformity to his wishes. He must make an earnest, not a simulated effort, with the managing body of the corporation, to induce remedial action on their part, and this must be made apparent to the court. If time permits, or has permitted, he must show, if he fails with the directors, that he has made an honest effort to obtain action by the stockholders as a body, in the matter of which he complains. And he must show a case, if this is not done, where it could not be done, or it was not reasonable to require it."

The *Hawes* case was followed by *Huntington* v. *Palmer*, 104 U.S. 482, 483-484, and *Dempfel* v. *Ohio and Mississippi R. Co.*, 110 U.S. 209, 210-211.

In the case at bar, no demand was made, or even contemplated, by Respondent as required by the consistent decisions of this Court and Rule 23(b). Respondent had nothing to lose and everything to gain by making a prior demand on Atlantic's Board of Directors. If such a demand had been made and Atlantic's Board had been advised of remedial action deemed necessary by Respondent, it is quite possible that there would be no need for these Petitioners to seek relief in the District Court or in this Court now. For, if Respondent had made a demand on Atlantic's Board seeking specific remedial steps and that demand had been refused, then, clearly, Respondent would have been justified in bringing a derivative action. But, as has been shown, Respondent did not seek the proper remedy or exhaust the remedies provided for him. As a result, his action, and the decision of the Court of Appeals herein, is contrary to thi Court's decisions in *Hawes*

and the other cases cited above and the intent and purpose of Rule 23(b).

It is uniformly held that courts will not entertain a derivative suit by stockholders on behalf of a corporation unless it clearly appears that all remedies within the corporation itself have been resorted to in vain. *Hawes* v. *City of Oakland*, 104 U.S. 450, 460-461; *Greenwood* v. *Union Freight R. Co.*, 105 U.S. 13, 15-16; *Cohen* v. *Industrial Finance Corporation*, 44 F.Supp. 491, 494-495 (S.D. N.Y. 1942); *Rogers* v. *American Can Co.*, 187 F.Supp. 532, 537 (D. N.J. 1960). And the Courts constantly stress that required demand upon corporate directors and shareholders is not a mere formality but must be an earnest effort to obtain action. *Lucking* v. *Delano*, 129 F.2d 283, 285-286 (6th Cir. 1942).

The foregoing prerequisite of prior demand upon a board of directors, before a shareholders' derivative action, cannot be dispensed with in such cursory fashion as Respondent admits he has done in this case. *City of Quincy* v. *Steel*, 120 U.S. 241, 247. There this Court said:

> "The rule [former Equity Rule 94] also requires that he must set forth with particularity his efforts to secure action on the part of the managing directors or trustees of the corporation of which he is a member, and, if necessary, of the shareholders, and the causes of his failure to obtain such action. . . ."

The reasons for the demand requirement upon corporate directors or shareholders, as a condition precedent to the maintenance of a derivative action, are important. If every shareholder were allowed to bring suit at his individual pleasure, the directors would find themselves harassed by a multiplicity of suits, and the courts would be swamped with endless litigation. In addition to guard-

ing against vexatious suits, the demand requirement facilitates authoritative management decisions without harassment and minimizes judicial interference in internal corporate affairs. Moreover, in many cases, such as the instant case, failure to make demand would be unjust and inequitable in subjecting Atlantic and other defendants to litigation and the substantial expenses incurred therewith. Also, the courts have emphasized in their decisions that the possibility of narrowing the issues or shortening the trial are additional reasons supporting the requirement of a prior demand upon the corporate directors and shareholders before a single shareholder institutes an action. *Lucking* v. *Delano*, 117 F.2d 159, 160 (6th Cir. 1941); *Haffer* v. *Voit*, 219 F.2d 704, 705 (6th Cir. 1955); *Group of Boston & P.R.C. Stockholders* v. *Interstate Commerce Commission*, 133 F.Supp. 488, 492-493 (E.D. Va. 1955); *Levitan* v. *Stout*, 97 F.Supp. 105, 113-116 (W.D. Ky. 1951).

In the case at bar, the record clearly shows that Atlantic's Board of Directors gave attention to the very matter upon which the complaint is based and took remedial action including a guaranty against loss. Respondent made no demand on the Board of Directors for any remedial action and gave no indication whether he was satisfied with remedial action that did take place. In fact, he admits he never even considered filing a demand. (Appendix D, p. 51). He never even considered the remedial action that was taken by Atlantic's Board of Directors, although a report thereon was transmitted to him approximately two months prior to the filing of his amended complaint. That such a complainant is entitled to ignore Rule 23(b) and go directly to court stultifies not only the intent and purpose of Rule 23(b) but all equitable principles upon which shareholder remedial procedures are based.

III. Failure to Follow Decisions of This Court, a Conflict in the Circuit Courts and Inconsistent Holdings in the District Courts Require Clarification of Rule 23(b) by This Court.

The decision below will create a most inequitable situation for corporations and their boards of directors. It will enable shareholders completely to evade the demand requirement set forth in Rule 23(b) and thus flood federal as well as state courts with litigation, much of which can be avoided if the Rule is reinstated to its full purpose by reversal of the decision of the Court of Appeals and reinstatement of the District Court's decision.

The complaint must show that plaintiff has made "an earnest, not a simulated effort." *Hawes* v. *City of Oakland*, 104 U.S. 450, 461. It must appear that plaintiff has done all that is reasonably expected of him; merely addressing a complaint to the board without any further attempt to induce action is not sufficient. *City of Quincy* v. *Steel*, 120 U.S. 241, 246-247; *Long* v. *Stites*, 88 F.2d 554, 555-556 (6th Cir. 1937). The complaint should show that the matters complained of were particularly brought to the attention of the directors and shareholders and that action to remedy the alleged conditions was specifically requested or demanded of them. *Isaac* v. *Milton Mfg. Co.*, 33 F.Supp. 732, 735-736 (M.D. Pa. 1940). And the filing of a complaint in court does not constitute a sufficient demand upon a board of directors in accordance with Rule 23(b). *Lucking* v. *Delano*, 117 F.2d 159, 160 (6th Cir. 1941).

If plaintiff has made no demand on the directors, Rule 23(b) provides that he must allege with particularity in his court complaint "the reasons for not making such effort." The bulk of the federal court decisions deal with this issue. The court, in passing upon the sufficiency of

the allegations, "should consider the whole complaint, not merely the paragraph in which the pleader summarizes his reasons for not demanding action by the directors or stockholders." *Cohen* v. *Industrial Finance Corp.*, 44 F. Supp. 491, 495 (S.D.N.Y. 1942). And contrary to the decision of the Court of Appeals herein, mere general averments that the directors are hostile to plaintiff or that demand would be useless and futile are not enough. *Lucking* v. *Delano*, 129 F.2d 283, 285-286 (6th Cir. 1943). And also contrary to the Court of Appeals decision herein, charges, in general terms, of Board member complicity in the wrongs complained are not sufficient to excuse a proper prior demand upon the Board of Directors. *Ziegler* v. *Lake St. Elev. R. Co.*, 76 Fed. 662 (7th Cir. 1896); *Shimer* v. *Milton Mfg. Co.*, 10 F.Supp. 943 (M.D. Pa. 1935); *Guth* v. *Groves*, 44 F.Supp 851 (S.D. N.Y. 1942).

Some courts have stated that prior demand upon directors or shareholders for remedial action will be excused in circumstances which prove that a demand would be "unavailing", "futile", or an "idle ceremony". However, the application of these nebulous criteria is a matter for wise judicial discretion. And, where, as here, testimony is before the District Court disproving such circumstances, the allegations of the complaint reciting such adjectives are clearly refuted. (Appendix D, p. 51-52.)

A conflict exists in the decisions of the Circuit Courts of Appeals with respect to the question of what constitutes proof of the futility of making a demand on shareholders. The Court of Appeals below held as follows (Appendix A, p. 24-25):

> "While the District Court did not reach that point, we see at once the futility of any such importunity upon the shareholders. With Scurlock and Sloan holding 40% of the voting stock, even without con-

sideration of the stockholdings of their associates, it would be costly business in time and money for the smaller holders to compel the corporation to protect its rights. The stock is widely distributed, and the convening of a sufficient number of the remainng 60% for a discussion and vote would certainly not be readily feasible."

Petitioners respectfully submit that, if large stockholders or a multiplicity of shareholders are a sufficient reason to excuse a plaintiff from making a demand upon the shareholders of a corporation, then a prior demand requirement would not be in the Federal Rules of Civil Procedure. It is a matter of judicial notice that there are a multitude of corporations with shareholders scattered throughout the country and the world. In *Haffer* v. *Voit*, 219 F.2d 704, 705 (6th Cir. 1955), the Court of Appeals stated that the mere fact that the other stockholders were widely scattered and that a demand upon them would involve expenses and delay, does not excuse the making of such a demand. See also *Quirke* v. *St. Louis-San Francisco Ry. Co.*, 277 F. 2d 705, 707 (8th Cir. 1960) and, contra, *Gottesman* v. *General Motors Corp.*, 268 F.2d 194, 197 (2d Cir. 1959). The Court of Appeals decision clearly conflicts with these decisions.

Furthermore, it has been held that the ownership of 40% of the voting stock of a corporation is not, as a matter of law, equivalent to full power over a board of directors, and that, in such a situation, plaintiff erred in not making a demand upon the board as a condition precedent to the maintenance of the suit. In so holding, the Court emphasized the small inconvenience in carrying out the demand requirement. *Levitan* v. *Stout*, 97 F. Supp., 105, 114-116 (W. D. Ky. 1951).

It is clear, however, that the District and Circuit Courts of Appeals have not been consistent in their holdings as to when a demand is and is not required. It has been held that, despite the allegations of the plaintiff which claim the utter absurdity of making a demand, a demand must nevertheless be made. *Squair* v. *Lookout Mountain Company*, 42 Fed. 729, 732-733 (C.C.E.D. Tenn 1890.) No case has been found, other than the opinion of the Court of Appeals herein, rejecting findings of a District Court based upon sworn testimony in favor of general allegations. It has been held that, merely because a majority of the directors are claimed to be implicated in the alleged fraud on the corporation, this does not excuse the necessity of a demand upon the entire board as a condition precedent to maintaining a suit in court. *Watson* v. *United States Sugar Refinery*, 68 Fed. 769, 773 (9th Cir. 1895). Nor will "vague and general averments of complicity on the part of the directors in the wrong against which relief is sought" bring plaintiff within the exception to the rule. *Ziegler* v. *Lake St. Elev. R. Co.*, 76 Fed. 662, 663 (7th Cir. 1896).

The decision of the Court of Appeals is in direct conflict with the *Watson* and *Ziegler* decisions, and subverts and sets aside the proper construction of Rule 23(b), as interpreted in this Court's construction of the similar equity rule in *Hawes* and *Quincy*. While these decisions pre-date the Federal Rules of Civil Procedure, there can be no doubt that those rules are a codification of the law set forth by the circuit courts of appeals in *Watson* and *Ziegler* and by this Court in *Hawes*, *Quincy*, and *Delaware & Hudson*. The District Court herein followed these decisions, and the Court of Appeals in its decision rejected them. This Court should reinstate the District Court's decision in order that the long-established rules of law, as codified in Rule 23(b), may be restored to their full intent and force in the Federal

courts, and in the state courts which follow this Rule's requirements and its purposes.

For this Court to refuse to grant the writ prayed for herein would be to abdicate its responsibility for the administration of federal procedure by allowing the nullification of the sound principle of judicial administration set forth in Rule 23(b) and further to burden the federal, as well as state, courts with a flood of unwarranted litigation.

Conclusion

For the foregoing reasons, the petition for a writ of certiorari should be granted.

Respectfully submitted,

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